

AR60

PERFECT FRY

REPORT 1998

CORPORATION

Winspear Business Reference Room
University of Alberta
1-18 Business Building
Edmonton, Alberta T6G 2R6



CORPORATE PROFILE

Perfect Fry Corporation is a public company headquartered in Calgary, Alberta, Canada. The aggressive pioneer spirit is a cornerstone in Perfect Fry's entrepreneurial quest for success.

The company manufactures counter-top deep fryers with built-in air filtration and fire prevention systems. The super efficient Perfect Fry is slightly bigger than a microwave oven.

Perfect Fry's market niche is fast food retailers who sell popular tasty deep fried foods at snack bars, food kiosks, sport & recreation outlets, concession stands, and convenience stores.

Perfect Fry's main sales force is an international network of independent distributors and dealers supported by targeted marketing and sales promotion programs.

Perfect Fry offers investors the basic elements for equity growth.

- Experienced management, with incentive to succeed.
- Dedicated employees with a stake in the company's future.
- Proven products serving a strong consumer demand: patented and continuously updated by research and development.
- A rapidly expanding distribution network.
- Access to capital to finance rapid growth.
- A production, marketing, distribution plan that is carving a profitable niche in the gigantic world-wide fast food industry.

1998 HIGHLIGHTS

- 1) Successful launch of the PFC Model Fryer.
- 2) Technological advances in electronics and filtration.
- 3) Continued expansion of the distributor network in the USA.
- 4) Continued sales success in Australia.
- 5) Developing distribution in South Africa and Spain.

PERFECT FRY
The Profit-maker



PFC MODELS:

- Wide range of cooking capacities
- State of the art electronic controls

ANNUAL MEETING

Perfect Fry Corporation's Annual Meeting for fiscal year 1998: April 26, 1999 at 9:00 a.m. at 3700, 400 - 3rd Avenue SW, Calgary, Alberta, Canada.

STOCK EXCHANGE LISTING

Perfect Fry Corporation, symbol PNM, is listed on the Alberta Stock Exchange in Calgary.
USA 12G3-2 (b) Exemption Number 82-1609.

LETTER FROM THE CHAIRMAN AND PRESIDENT

In 1998 Perfect Fry Corporation has been building the foundation for the future. We experienced another year of significant changes. Under new management in 1998, we had the opportunity to evaluate the fundamentals in our product, our distribution and our plant infrastructure. A broader, more reliable distributor base continues to be established, production capabilities (facilities) have been expanded, more international approvals were gained, the technology in the new PFC line of fryers was enhanced and advanced, and the internal structure of the company was reorganized.

Development of the distribution network continues to be the main focus of the sales department. Perfect Fry sales representatives visit each distributor to develop a close relationship and determine the distributor's ability to promote, service, and support the Perfect Fry line of equipment. This relationship building requires a significant investment in time, energy and finances. Establishing a successful relationship requires a minimum of 6 months and may take as long as 2 years to develop. The establishment of each successful relationship ensures that Perfect Fry will have a strong distribution base for years to come. Most of the distributors have been in the business for many years and in a lot of cases are multi-generational.

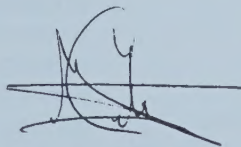
During 1998 we delivered the first of our new PFC series fryers. This enhanced line now gives the customer a broad range of cooking capacities to choose from. In general the more power or wattage into the fryer the more capacity output. Perfect Fry now provides the highest capacity self-contained counter-top fryer on the market. 70% of the sales of Perfect Fry Corporation is this high capacity PFC 5700 model. Distributors and customers who had experience with our prior model were somewhat skeptical about the technological advances in the computerized electronics and the completely new physical design of the fryer. This skepticism has now been greatly relieved due to a heightened comfort level by the distributors, arising from both familiarity with the product and the successful use and ease of sales of the new fryers.

Perfect Fry is poised and ready for the new millennium. We are grateful to the staff, the distributors, the suppliers, the customers and most particularly to the shareholders for their support and patience. Morale is better than ever and we are enveloped by a sense of anticipation as we look to the future.

On behalf of the Board,



Jack Senior
Chairman



Gary Calderwood
President and CEO

MANAGEMENT DISCUSSION AND ANALYSIS

SALES AND MARKETING

Although our sales were slightly lower than previous years, no one distributor represented more than 13% of fryer sales. In 1995 one distributor represented 75% of total sales, in 1996 they had 50% of sales and in 1997 it was 30%. This year the average distributor represented 5% of total sales. This is a huge accomplishment, ensuring Perfect Fry's strength as an independent company. Broadening and strengthening the distributor base was costlier and more time consuming than was anticipated. Travel was a key expenditure in this area. Searching out and then evaluating a potential distributor is a long arduous process. The results, however, are very encouraging.

Perfect Fry Distributors & Dealer Locations

At January 31	<u>1999</u>	<u>1998</u>
Distributors	38	33
Branches	22	16
Dealers	40	-
International	5	5

FINANCIAL CONDITION

The amortization of development costs and capital assets has been added back to give a positive cash flow of \$33,000. Investments during the year included additions to development costs of \$209,000, capital assets of \$61,000 and inventory and accounts receivable of \$165,000. These investments reflect the Company's confidence in the new product series and the enlarged distributor base.

The Year 2000 Issue arises because many systems use two digits rather than four to identify a year. Further information about this issue has been included in the Notes to Consolidated Financial Statements, Note 10.

Perfect Fry recognized the Year 2000 issue as a potential problem 3 years ago and has taken steps to upgrade the computer systems. In 1997 and 1998 investments totaling \$50,000 were made to upgrade the computer hardware and software. These investments were capitalized to fixed assets. Letters of

compliance have been received from all the software suppliers. At this point in time all systems have been tested and a backup plan is in existence for January 1, 2000.

Even though Perfect Fry has reduced the internal risk associated with the Year 2000 problem, there may still be a risk from unforeseen problems with third parties with whom the Company deals.

DEVELOPMENTS & OPERATIONS

In July of 1998, after 13 years at the current location, the bay next door became available. The existing production facilities were extremely tight, and although we were not eager to increase the overhead, the opportunity of expansion without moving to another location was considered a positive step towards future positioning. The immediate reward of expansion was the ability for the production staff to reorganize thereby increasing production capabilities and efficiencies.

The new PFC model fryer now meets stringent regulations throughout North America and the World. The CE and EMC marks for worldwide recognition are now complete.

Perfect Fry leads the industry in technology. The overall design and function of the fryers is significantly more advanced than the competition. The air filtration system has been redesigned for higher efficiency. The increased cooking capacity from the higher power fryers is gaining significant success in the marketplace. Perfect Fry has designed and now manufactures it's own fire suppression system. This gives the company design and cost control capabilities which most food equipment manufacturers are unable or unwilling to attain.

More good news, Prefect Fry has realigned the expenditures to prioritize efforts in the production and sales departments. This realignment, particularly in salary dollars, is another step towards building a stronger company.

Consolidated Financial Statements of

PERFECT FRY CORPORATION

Years ended October 31, 1998 and 1997

MANAGEMENT'S REPORT TO THE SHAREHOLDERS

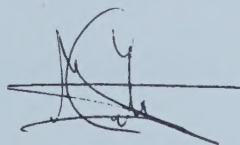
Management is responsible for the production of the Company's financial statements. Management believes that the financial statements fairly reflect the form and substance of transactions and that the financial statements reasonably present the Company's financial condition and results of operations in conformity with generally accepted accounting principles. Management has included in the Company's financial statements amounts based on estimates and judgments that it believes are reasonable under the circumstances.

The independent auditors appointed by the shareholders of the Company have audited the Company's financial statements in accordance with generally accepted auditing standards and they provide an objective, independent review of the fairness of reported operating results and financial position.

The Board of Directors of the company has an Audit Committee which meets with financial management and the independent auditors to review accounting, auditing, internal accounting controls and financial reporting matters.



Jack F. Senior
Chairman of the Board



Gary G. Calderwood
President and CEO

AUDITORS' REPORT TO THE SHAREHOLDERS

We have audited the consolidated balance sheets of Perfect Fry Corporation as at October 31, 1998 and 1997 and the consolidated statements of operations and retained earnings and changes in financial position for the years then ended. These financial statements are the responsibility of the company's management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with generally accepted auditing standards. Those standards require that we plan and perform an audit to obtain reasonable assurance whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation.

In our opinion, these consolidated financial statements present fairly, in all material respects, the financial position of the company as at October 31, 1998 and 1997 and the results of its operations and the changes in its financial position for the years then ended in accordance with generally accepted accounting principles.

KPMG LLP

Chartered Accountants

Calgary, Canada
December 11, 1998

PERFECT FRY CORPORATION

Consolidated Balance Sheets

October 31, 1998 and 1997

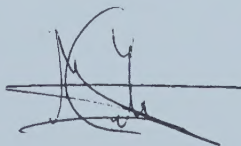
	1998	1997
Assets		
Current assets:		
Cash	\$ —	\$ 64,863
Accounts receivable	426,668	384,690
Inventories (note 2)	942,557	819,440
Prepaid expenses	29,202	80,386
	1,398,427	1,349,379
Capital assets (note 3)	165,917	148,487
Deferred product development costs	738,149	645,268
	\$ 2,302,493	\$ 2,143,134
Liabilities and Shareholders' Equity		
Current liabilities:		
Bank indebtedness (note 4)	\$ 279,104	—
Accounts payable and accrued liabilities	192,596	185,558
	471,700	185,558
Shareholders' equity:		
Share capital (note 5)	1,433,471	1,433,471
Retained earnings	397,322	524,105
	1,830,793	1,957,576
Commitment (note 8)		
	\$ 2,302,493	\$ 2,143,134

See accompanying notes to consolidated financial statements.

On behalf of the Board:



Director



Director

PERFECT FRY CORPORATION

Consolidated Statements of Operations and Retained Earnings

Years ended October 31, 1998 and 1997

	1998	1997
Revenue	\$ 1,681,360	\$ 1,718,260
Costs and expenses:		
Operating, selling and administrative	1,648,639	1,516,853
Amortization:		
Deferred product development costs	115,920	106,922
Capital assets	43,584	32,800
Research and development	—	31,961
	1,808,143	1,688,536
Net earnings (loss)	(126,783)	29,724
Retained earnings, beginning of year	524,105	494,381
Retained earnings, end of year	\$ 397,322	\$ 524,105
Loss per share	\$ (0.01)	\$ —

See accompanying notes to consolidated financial statements.

PERFECT FRY CORPORATION

Consolidated Statements of Changes in Financial Position

Years ended October 31, 1998 and 1997

	1998	1997
Cash provided by (used in):		
Operations:		
Net earnings (loss)	\$ (126,783)	\$ 29,724
Items not affecting cash:		
Amortization of deferred product development costs	115,920	106,922
Amortization of capital assets	43,584	32,800
	32,721	169,446
Changes in non-cash operating working capital	(106,873)	312,060
	(74,152)	481,506
Financing:		
Decrease in long-term debt	—	(118,500)
Issue of share capital	—	76,919
	—	(41,581)
Investing:		
Additions to deferred product development costs	(208,801)	(288,857)
Additions to capital assets	(61,014)	(96,622)
	(269,815)	(385,479)
Increase (decrease) in cash	(343,967)	54,446
Cash, beginning of year	64,863	10,417
Cash (bank indebtedness), end of year	\$ (279,104)	\$ 64,863

See accompanying notes to consolidated financial statements.

PERFECT FRY CORPORATION

Notes to Consolidated Financial Statements

Years ended October 31, 1998 and 1997

1. Significant accounting policies:

(a) Basis of presentation:

These consolidated financial statements include the accounts of the Company and those of its subsidiary companies all of which are wholly-owned.

(b) Inventories:

Inventories are recorded at the lower of cost and net realizable value. Cost is determined using the weight-average method and includes material, direct labour and overhead.

(c) Capital assets:

Capital assets are recorded at cost net of applicable government grants. Amortization is provided as follows:

	Basis	Rate
Office and equipment	Declining-balance	20% to 30%
Leasehold improvements	Straight-line	Over the term of the lease
Other assets	Declining-balance	25%

(d) Deferred product development costs:

Product development costs are expensed unless they meet specific criteria related to technical, market and financial feasibility, in which case they are deferred and amortized on a straight-line basis over ten years. All research costs are expensed as incurred.

During the year management increased its estimate of the useful lives of the deferred development costs to ten years from three years. This change has been accounted for on a prospective basis.

The value of the residual unamortized balance of deferred product development costs is assessed at least annually with reference to the projected cash flows, undiscounted, related thereto.

(e) Measurement uncertainty:

The preparation of financial statements in accordance with generally accepted accounting principles requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities, the disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenue, costs and expenses during the reporting period. In the consolidated financial statements of the Company, the most significant areas for which management is required to make near-term estimates is in the assessment of the net realizable value of inventories and the net recoverable value of deferred development costs, patents and processes and goodwill. Actual amounts could differ from those estimates.

PERFECT FRY CORPORATION

Notes to Consolidated Financial Statements

Years ended October 31, 1998 and 1997

2. Inventories:

	1998	1997
Finished units	\$ 198,055	\$ 352,570
Parts	744,502	466,870
	<u>\$ 942,557</u>	<u>\$ 819,440</u>

3. Capital assets:

1998	Cost	Accumulated amortization	Net book value
Office and equipment	\$ 260,200	\$ 117,965	\$ 142,235
Leasehold improvements	36,914	17,381	19,533
Other assets	70,299	66,150	4,149
	<u>\$ 367,413</u>	<u>\$ 201,496</u>	<u>\$ 165,917</u>

1997	Cost	Accumulated amortization	Net book value
Office and equipment	\$ 208,712	\$ 78,961	\$ 129,751
Leasehold improvements	27,388	14,270	13,118
Other assets	70,299	64,681	5,618
	<u>\$ 306,399</u>	<u>\$ 157,912</u>	<u>\$ 148,487</u>

4. Bank indebtedness:

The Company has a bank operating credit facility of \$500,000. Advances under this facility bear interest at prime plus 1.25% and are secured by all assets of the business.

PERFECT FRY CORPORATION

Notes to Consolidated Financial Statements

Years ended October 31, 1998 and 1997

5. Share capital:

(a) Authorized:

Unlimited number of preferred and common shares.

(b) Issued:

	Number of common shares	Amount
Balance, October 31, 1996	9,431,351	\$ 1,356,552
Issued on exercise of warrants, for cash	192,297	76,919
Balance, October 31, 1997 and 1998	9,623,648	\$ 1,433,471

(c) Options:

At October 31, 1998 490,000 options to acquire common shares were outstanding with an exercise price of \$0.50 and expiring from time to time up to April 29, 2002. Of the options outstanding, 350,000 were issued to directors and officers of the Company.

(d) Earnings (loss) per share:

Earnings (loss) per share have been calculated using the monthly weighted average number of common shares outstanding during the year. The effects of the exercise of outstanding share options are not dilutive to earnings per share.

6. Export sales:

The Company's sales outside Canada totalled \$1,243,559 (1997 - \$1,164,674).

PERFECT FRY CORPORATION

Notes to Consolidated Financial Statements

Years ended October 31, 1998 and 1997

7. Income taxes:

The provision for income taxes differs from that which would be expected by applying statutory rates. A reconciliation of the differences is as follows:

	1998	1997
Net earnings (loss)	\$ (126,783)	\$ 29,724
Combined Federal and Provincial income tax rate	44.6%	44.6%
Computed income tax provision (recovery)	\$ (56,545)	\$ 13,000
Increase (decrease) resulting from:		
Loss carry forwards not recognized	41,295	—
Non-deductible amortization	11,500	11,500
Other	3,750	850
Recognition of loss carry-forwards not previously recognized	—	(25,350)
	\$ —	\$ —

The Company has non-capital losses for income tax purposes which may be carried forward to reduce taxable income in future years (subject to confirmation by income tax authorities). The losses expire as follows:

1999	\$ 139,000
2000	70,000
2001	416,000
2003	6,000
2005	33,000
	\$ 664,000

In addition the Company has aggregate tax pools, excluding the above non-capital losses, which exceed the net book value of the related capital assets available for deduction against future years taxable income in the amount of \$2,621,000.

The potential benefit of the above losses and timing differences has not been recognized in the financial statements.

PERFECT FRY CORPORATION

Notes to Consolidated Financial Statements

Years ended October 31, 1998 and 1997

8. Commitment:

The Company is committed to future annual operating lease payments for facilities not including operating costs, over the next five years as follows:

1999	\$ 50,730
2000	52,420
2001	52,420
2002	52,420
2003	52,420

9. Financial instruments:

Financial instruments of the Company include cash, accounts receivable, accounts payable and accrued liabilities and bank indebtedness. The fair values of all financial instruments are estimated to approximate their carrying values due to their short-term nature.

10. Uncertainty due to the Year 2000 Issue:

The Year 2000 Issue arises because many computerized systems use two digits rather than four to identify a year. Date-sensitive systems may recognize the year 2000 as 1900 or some other date, resulting in errors when information using year 2000 dates is processed. In addition, similar problems may arise in some systems which use certain dates in 1999 to represent something other than a date.

The effects of the Year 2000 Issue may be experienced before, on, or after January 1, 2000 and, if not addressed, the impact on operations and financial reporting may range from minor errors to significant system failure which could affect an entity's ability to conduct normal business operations. It is not possible to be certain that all aspects of the Year 2000 Issue affecting the entity, including those related to the efforts of customers, suppliers or other third parties, will be fully resolved.

CORPORATE DIRECTORY

BOARD OF DIRECTORS

Jack F. Senior, Chairman
President,
Speedi Gourmet Ltd.
Vancouver, B.C.

Gary G. Calderwood
President and CEO,
Perfect Fry Corporation

P. Glenn Calderwood
Owner-Manager & Director,
Private Corporations
Calgary, Alberta

William O. Wright
President,
Guidance Financial Consultants
Wichita, Kansas

LEGAL COUNSEL

Macleod Dixon
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OFFICERS

Gary G. Calderwood
President, CEO,
Secretary-Treasurer

Cynthia C. Horne
Chief Financial Officer

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INVESTOR RELATIONS

Cynthia C. Horne

STOCK EXCHANGE LISTING

Alberta Stock Exchange,
Symbol: PNM

As of October 31, 1998 there
were 9,623,648 shares issued
and outstanding.



PERFECT FRY

REPORT 1998

CORPORATION

PRINTED IN CANADA

